What are mutual funds?

It is a trust that collects money from a number of investors who share a common investment objective and invests the same in equities, bonds, money market instruments and/or other securities. And the income / gains generated from this collective investment is distributed proportionately amongst the investors after deducting applicable expenses and levies, by calculating a scheme’s “Net Asset Value” or NAV. Simply put, the money pooled in by a large number of investors is what makes up a Mutual Fund.

Here’s a simple way to understand the concept of a Mutual Fund Unit.  
Let’s say that there is a box of 12 chocolates costing ₹40. Four friends decide to buy the same, but they have only ₹10 each and the shopkeeper only sells by the box. So the friends then decide to pool in ₹10 each and buy the box of 12 chocolates. Now based on their contribution, they each receive 3 chocolates or 3 units, if equated with Mutual Funds.  
And how do you calculate the cost of one unit? Simply divide the total amount with the total number of chocolates: 40/12 = 3.33.  
So if you were to multiply the number of units (3) with the cost per unit (3.33), you get the initial investment of ₹10.

This results in each friend being a unit holder in the box of chocolates that is collectively owned by all of them, with each person being a part owner of the box.

Next, let us understand what is “Net Asset Value” or NAV. Just like an equity share has a traded price, a mutual fund unit has Net Asset Value per Unit. The NAV is the combined market value of the shares, bonds and securities held by a fund on any particular day (as reduced by permitted expenses and charges). NAV per Unit represents the market value of all the Units in a mutual fund scheme on a given day, net of all expenses and liabilities plus income accrued, divided by the outstanding number of Units in the scheme.

Mutual funds are ideal for investors who either lack large sums for investment, or for those who neither have the inclination nor the time to research the market, yet want to grow their wealth. The money collected in mutual funds is invested by professional fund managers in line with the scheme’s stated objective. In return, the fund house charges a small fee which is deducted from the investment. The fees charged by mutual funds are regulated and are subject to certain limits specified by the Securities and Exchange Board of India (SEBI).

India has one of the highest savings rate globally. This penchant for wealth creation makes it necessary for Indian investors to look beyond the traditionally favoured bank FDs and gold towards mutual funds. However, lack of awareness has made mutual funds a less preferred investment avenue.

Mutual funds offer multiple product choices for investment across the financial spectrum. As investment goals vary – post-retirement expenses, money for children’s education or marriage, house purchase, etc. – the products required to achieve these goals vary too. The Indian mutual fund industry offers a plethora of schemes and caters to all types of investor needs.

Mutual funds offer an excellent avenue for retail investors to participate and benefit from the uptrends in capital markets. While investing in mutual funds can be beneficial, selecting the right fund can be challenging. Hence, investors should do proper due diligence of the fund and take into consideration the risk-return trade-off and time horizon or consult a professional investment adviser. Further, in order to reap maximum benefit from mutual fund investments, it is important for investors to diversify across different categories of funds such as equity, debt and gold.

While investors of all categories can invest in securities market on their own, a mutual fund is a better choice for the only reason that all benefits come in a package.

why you should invest in Mutual Funds

Earn. Save. Spend. This is the cycle of money that we live by every month, if not every day, of our lives. By now, we’re sure you know the importance of saving. Perhaps, you’ve even realized the significance of investing. If not, here’s a quick primer - when you save, your money sits idle. When you invest, your money multiplies.  
  
Your investment choice can, obviously, significantly impact the rate at which your money compounds. While there are enough opinions on what you should be doing with your money, here are 7 reasons why mutual funds should definitely be a part of your wealth building portfolio.  
  
**1. Higher returns**  
Isn’t this what all of us seek from our investments? Mutual funds provide the right avenue for investing in a variety of market-linked instruments, which have time and again delivered superior returns compared to other traditional investment options. Debt funds have consistently beaten Fixed Deposit (FD) returns, and with bank interest rates going south, they present a good investment choice for investors with lower risk appetites. For the more adventurous investors, equities (shares) present a great investment avenue, for higher, inflation-beating returns. And investing in equities through mutual funds is an excellent way to enjoy the higher returns, but with much lesser risk, thanks to rupee-cost averaging, portfolio diversification and many other factors. Data reveals that equity funds have delivered around 11-15% returns over the last 10 years. With inflation averaging at 4-6%, you could get a head start on your savings, by identifying and investing in the right mutual funds today.  
  
**2. Professionally managed**  
Mutual funds are professionally managed by fund managers, whose every day job is to track the markets and manage investments. Fund managers identify the winning stocks to buy, when to buy them, and more importantly, when to sell them. They spend hours analysing the performance of companies, and if they fit the fund they manage. What’s more, all mutual funds are governed by SEBI, the industry body, and are highly secure and transparent. So, while earning is your job, investing it wisely and delivering high returns is the fund manager’s job. You can rest assured, knowing that when you invest in the right mutual fund, he/she is likely to manage your funds far better than you.  
  
**3. Disciplined investing**  
Habits are hard to break. Which is why we are advised to inculcate good habits. And what better habit could there be, than investing for your secure future? When you start a Systematic Investment Plan (SIP) in a mutual fund, you are committing to invest a certain amount on the same day of the month, consistently for a certain number of months/ years. Such a commitment instils in you the discipline to take a productive action towards your future. It becomes a fixed component of your monthly spend, around which all other expenses have to be factored. Your disposable income will be that which is left, after your mandatory expenses and investments are done. This way, you ensure that nothing comes in the way of your goals - neither a fancy dinner nor a shopping trip.   
  
**4. Less/ No lock-in**  
Almost all your traditional investing instruments come with long lock-in periods, which make it hard for you to get your money out, in times of emergencies. Mutual funds, on the other hand, broadly come with less, if not no, lock-in periods. Most funds do not have a lock-in period and give you the flexibility to redeem your money when you need it. Even tax-saving Equity Linked Savings Schemes (ELSS) come with a short lock-in of only 3 years. So you are saved the hassle of fixed, long lock-in periods, as seen in other investment options. Having said that, experts recommend that a fund should not be redeemed until the goal for which it was started is fulfilled, as the longer you stay invested, better are your chances for higher returns.   
  
**5. The fund with your name on it**  
Within the world of mutual funds there is a wide variety of investment choices to pick from - equity funds, debt funds, liquid funds, tax-saving funds etc. So, depending upon your profile, goal and preference, there are various funds that are ideal for you. Unlike a PPF or an NSC, where the rules are already laid down for you, here you can choose what type of fund you want, how long you want to stay invested, how much you want to invest, and much more. Just like how a tailor-made outfit is often a better fit for you than a ready-made garment, a personalized mutual fund portfolio with the right advisor is the best fit for your goals.  
  
**6. Diversification**  
We’ve all heard the adage “Don’t put all your eggs in one basket”. This is the premise of diversification. It means spreading your investments across asset classes and stocks, to reduce your risk. With mutual funds, you get the advantage of default diversification, as your fund manager invests across a variety of stocks. Sudden changes in one stock, are likely to be balanced out by the performance of other stocks in the fund. It is an ideal way to get a taste of the equity markets, but with lesser risk. Of course, it is important to not invest all your money in one mutual fund, and further lessen your risk by diversifying across different types of mutual funds. Consult your financial advisor on how to balance your portfolio by selecting the right mutual funds.  
  
**7. Convenience**  
And finally, investing in mutual funds is now a piece of cake. The whole process is offered online by many players in the industry. Starting a SIP or making an investment can be done in a matter of few clicks. Even tracking the performance of your investments can be done easily online. You can set up a bank mandate for monthly investments and set your SIPs on auto-pilot mode, so that you are even saved the hassle of manually investing every month. The SIP amount is automatically debited every month from your account. In short, mutual funds today, provide the right ground for investing with the least effort, and with the potential for maximum returns.

**What are the different types of mutual fund schemes?**

**Schemes according to Maturity Period:**

A mutual fund scheme can be classified into open-ended scheme or close-ended scheme depending on its maturity period.

**Open-ended Fund/ Scheme:**

An open-ended fund or scheme is one that is available for subscription and repurchase on a continuous basis. These schemes do not have a fixed maturity period. Investors can conveniently buy and sell units at Net Asset Value (NAV) related prices which are declared on a daily basis. The key feature of open-end schemes is liquidity.

**Close-ended Fund/ Scheme:**

A close-ended fund or scheme has a stipulated maturity period e.g. 5-7 years. The fund is open for subscription only during a specified period at the time of launch of the scheme. Investors can invest in the scheme at the time of the initial public issue and thereafter they can buy or sell the units of the scheme on the stock exchanges where the units are listed. In order to provide an exit route to the investors, some close-ended funds give an option of selling back the units to the mutual fund through periodic repurchase at NAV related prices. SEBI Regulations stipulate that at least one of the two exit routes is provided to the investor i.e. either repurchase facility or through listing on stock exchanges. These mutual funds schemes disclose NAV generally on weekly basis.

**Schemes according to Investment Objective:**

A scheme can also be classified as growth scheme, income scheme, or balanced scheme considering its investment objective. Such schemes may be open-ended or close-ended schemes as described earlier. Such schemes may be classified mainly as follows:

**Growth / Equity Oriented Scheme**

The aim of growth funds is to provide capital appreciation over the medium to long- term. Such schemes normally invest a major part of their corpus in equities. Such funds have comparatively high risks. These schemes provide different options to the investors like dividend option, capital appreciation, etc. and the investors may choose an option depending on their preferences. The investors must indicate the option in the application form. The mutual funds also allow the investors to change the options at a later date. Growth schemes are good for investors having a long-term outlook seeking appreciation over a period of time.

**Income / Debt Oriented Scheme:**

The aim of income funds is to provide regular and steady income to investors. Such schemes generally invest in fixed income securities such as bonds, corporate debentures, Government securities and money market instruments. Such funds are less risky compared to equity schemes. These funds are not affected because of fluctuations in equity markets. However, opportunities of capital appreciation are also limited in such funds. The NAVs of such funds are affected because of change in interest rates in the country. If the interest rates fall, NAVs of such funds are likely to increase in the short run and vice versa. However, long term investors may not bother about these fluctuations.

**Balanced Fund:**

The aim of balanced funds is to provide both growth and regular income as such schemes invest both in equities and fixed income securities in the proportion indicated in their offer documents. These are appropriate for investors looking for moderate growth. They generally invest 40-60% in equity and debt instruments. These funds are also affected because of fluctuations in share prices in the stock markets. However, NAVs of such funds are likely to be less volatile compared to pure equity funds.

**Money Market or Liquid Fund:**

These funds are also income funds and their aim is to provide easy liquidity, preservation of capital and moderate income. These schemes invest exclusively in safer short-term instruments such as treasury bills, certificates of deposit, commercial paper and inter-bank call money, government securities, etc. Returns on these schemes fluctuate much less compared to other funds. These funds are appropriate for corporate and individual investors as a means to park their surplus funds for short periods.

**Gilt Fund:**

These funds invest exclusively in government securities. Government securities have no default risk. NAVs of these schemes also fluctuate due to change in interest rates and other economic factors as is the case with income or debt oriented schemes.

**Index Funds:**

Index Funds replicate the portfolio of a particular index such as the BSE Sensitive index, S&P NSE 50 index (Nifty), etc These schemes invest in the securities in the same weightage comprising of an index. NAVs of such schemes would rise or fall in accordance with the rise or fall in the index, though not exactly by the same percentage due to some factors known as "tracking error" in technical terms. Necessary disclosures in this regard are made in the offer document of the mutual fund scheme.   
  
There are also exchange traded index funds launched by the mutual funds which are traded on the stock exchanges

## The Benefits of Having a Certified Financial Planner™

Creating a financial plan helps you see the big picture and set long and short-term life goals, a crucial step in mapping out your financial future. When you have a financial plan, it's easier to make financial decisions and stay on track to meet your goals. Working with a CFP® professional can secure your financial wellbeing and give you peace of mind and help you reach financial planning success.

### The Importance of Having a Financial Plan

Some people decide to do their own financial planning, but you may want to seek help from a Certified Financial Planner™ professional if you:

* Want to better manage your finances, but aren't sure where to start
* Don't have time to do your own financial planning
* Want a professional opinion about the plan you've developed
* Don't have sufficient expertise in certain areas such as investments, insurance, taxes or retirement planning
* Have an immediate need or unexpected life event

**2nd option:**

# Why do you need financial planning? Here are 7 things to know

Long-term financial goals need security and that can only be provided by taking an insurance plan.

In a bid to get good returns, we invest in various asset classes, ranging from equities to bonds to mutual funds. But we usually forget the other aspects of it. Should we look at only returns while making investments?

The fact is before investing, you should know your main financial goals, especially for what reason you want to invest your money. What purpose will that serve for you? Do you have sufficient funds to invest? What are your liabilities at present? Financial planning not only helps in building wealth, but also helps in securing your finances.

Here are six ways how financial planning can help you in financial matters during your lifetime:

**Secures financial conditions**  
Long-term financial goals need security and that can only be provided by taking an insurance plan. For a long-term financial goal, you need to think about the continuity of savings you need to do for that particular time period to achieve that goal, keeping in mind any mishappening which can occur during that stage. A planned goal always helps you in evaluating your insurance need, which helps in getting a cover for your liabilities.

**Helps in saving taxes**  
Financial planning helps you to invest smartly as certain funds provide dual benefit. One, getting good returns & secondly, helping you in savings taxes where you can save up to Rs 1.5 lakh under section 80C of the I-T Act. Various options like ELSS mutual funds, PPF, tax-free bonds, etc provide both tax benefit and capital appreciation.

**Helps in planning debt-free trips**  
If you have planned properly for your future goals like going on a vacation, you need not have to use your credit card or take a loan, which eventually increases your liability. In fact, prior savings will help you in growing your financial assets so that you could easily afford to go out for a vacation without opting for a debt and paying long-term EMIs. Small trips can be planned every two-three years if financial matters are planned properly.

**Helps in increasing net worth**  
While doing financial planning, your cash flows are properly managed from time to time which is analyzed in such a way that it shouldn’t get negative at any point of time while planning your future financial goals. This process helps in building your assets without increasing your liabilities (over and above your income level), which in-turn increases your net worth over a period of time.

**Guilt-free spending**  
Why not plan your monthly budget on a regular basis when it is a daily routine of your life? Many of us do not plan for it because of which we come into the category of spendthrifts where your expenses exceed your savings and therefore, you are not able to plan for a financial goal. Planning helps in avoiding unnecessary expenses which you tend to make during an unplanned monthly budget.

**Improves your standard of living**  
People who do financial planning and save money as per their financial goals are able to accumulate enough wealth for leading a comfortable life. Every goal, whether it is buying a house or buying a car, increases your net worth and upgrades your standard of living. A financial goal helps you grow your money in a logical and planned way.

**Helps in wealth creation**  
It is better to start planning today rather than buy things at the last moment and then keep paying the interest for the next 7 to 10 years or more. Let us understand this with the help of an example. Mr Kumar has just started his job in a multinational company and decided to buy a Rs 1 crore home for himself after 20 years. He started his investment in mutual fund schemes (assuming return at 15%). He needs to start saving Rs 6500 per month to achieve his desired goal in the next 20 years. Therefore, by investing only Rs.15.85 lakh approximately, he will be able to achieve his goal. This means that if you have started planning to buy a house today, you will probably get it at the end of 20th years at a lower cost than what you will actually pay for it.

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# Why Should I Invest?

There are only two ways to make money in our modern world:  by working, for yourself or someone else, and/or by having your assets work for you. If you keep your life savings in your back pocket or under a mattress, instead of investing, the money doesn't work for you and you'll never have more than what you save or receive through inheritance. Conversely, investors generate money by earning interest on what they set aside or by buying assets that increase in value.

It doesn't matter how you do it. Whether you invest in stocks, [bonds](https://www.investopedia.com/terms/b/bond.asp), [mutual funds](https://www.investopedia.com/terms/m/mutualfund.asp), [options](https://www.investopedia.com/terms/o/option.asp), [futures](https://www.investopedia.com/terms/f/futures.asp), [precious metals](https://www.investopedia.com/terms/p/preciousmetal.asp), real estate, a small business or a combination of assets, the objective is the same: to make investments that generate additional cash. As the old expression goes, "Money isn't everything but happiness alone can't keep out the rain." So, whether your goal is to send your kids to college or to retire on a yacht in the Mediterranean, investing is essential in getting where you want to go in life.

## Managing Investment Goals

Investment goals diverge, depending on age, income and outlook.  You can further sub-divide age into three categories, young and starting out, middle aged and family building, old and self-directed. These segments often miss their marks at the appropriate age, with middle-aged folks considering investments for the first time or the elderly forced to budget, employing the discipline they lacked as young adults.

Income provides as the natural starting point for investment planning because you can’t invest what you don’t have. The first career job issues a wake-up call for many young adults, forcing decisions about IRA contributions, savings or money market accounts, and the sacrifices needed to balance growing affluence with the desire for gratification. Don't worry too much about setbacks during this period, like getting overwhelmed by student loans and car payments, or forgetting that your parents no longer pay the monthly credit card bill.

Outlook defines the playing field on which we operate during our lifetimes and the choices that impact wealth management.  Family planning sits at the top of this list for many individuals, with couples figuring out how many kids they want, where they want to live, and how much money is needed to accomplish those goals. Career expectations often complicate these calculations, with the highly-educated enjoying increased earning power while those stuck in low level jobs are forced to cut back to make ends meet.

It’s never too late to become an investor. You may be well into middle age before realizing that life is moving quickly, requiring a plan to deal with old age and retirement. Fear can take control if waiting too long to set investment goals but that should go away once you set the plan into motion. Remember that all investments start with the first dollar, whatever your age, income or outlook.  That said, those investing for decades have the advantage, with growing wealth allowing them to enjoy the lifestyle that others cannot afford.

How much amount you want to invest

Suppose you want to invest 2,000 to 5,000 per month in stock market and finding a way to do it then here is the game plan.

There are two kinds of stock that we trade.

1. **BlueChip Stocks** and **Too Big to Fail stocks** *( well-established and financially sound company that has operated for many years and has a market capitalization in the billions)*
2. **Other stocks** ( Micro small cap, Midcap, Small cap) : High risk stocks.

We are going to invest only in **BlueChip Stocks** and **Too Big to Fail stocks** so that we can reduce the risk and expect for better returns for short term and long term gains.

This is not the end, before investing a single penny in stock market you should know ‘when to enter the stock ( at which price)’ and ‘when to exit the stock’ in order to make sufficient gains. The stock you are choosing must have good cash flows, lesser debt, better ROE and ROCE, considerable earnings, well diversified business model, better shareholding pattern, a good book value, better technicals also so that they can direct you when to enter the stock and when to exit.  
**(Important: Almost all the stocks mentioned above have already provided 20–30% returns to the investors from Jan 1, 2017 till now)**

***Quick steps to follow for better investment plan.***

1. **Open a demat account** : You can open your demat account in a good brokerage firm like edelweiss, kotak securities, sharekhan etc. They charge almost same.
2. **Contribute every month** : Take a fix/variable amount every month, choose 1 or 2 stock ( the way I explained above ) and BUY those stocks.
3. **BUY SELL and repeat** : Do it for 6–12 months or longer period, meanwhile if you think some of the stock is giving you good returns the SELL them all and add some other as per market trend.

**Benefits :**

* At the end the 6–12 months you will have a healthy stock portfolio with better future growth.
* You will get introduced with daily market activities.
* Apart from good returns, almost all the quality stocks give dividend in the form of cash, it would be added in your savings regularly.
* Stock split will increase the number of shares in your demat account automatically.
* A better savings will be saved in the form of securities ( stocks) which can be liquidate every time.

According to economic times 2017 may be the best time to invest in stock market because BULLs are already in charge and SENSEX is heading towards 34,000 mark.

How much time you want to invest?

One of the most important considerations before choosing an investment avenue is the expected “**time horizon**”, i.e. time in days, months or years that an investor intends to stay invested.

And why is this so important?

There are two types of people that make money on the stock market: **Investors** and **Speculators**.

* **Investors** are people that pick a stock that's relatively low, relatively secure, and buy the stock for the long run, 5, 10 years or more. Warren Buffet said his ideal period for investing is forever. Basically, a well run company should always be a good investment.
* **Speculators** go for the fluctuations in stock prices. Day traders, Options, etc. It's risky business and you'll be able to lose a lot of money in a short term.

There's always a risk when you invest your money, so go with MrChrister's advise to start with a simulator.

All investments should ideally result from a financial or investment plan. Such plans usually indicate how long it would take for a financial objective to be met.

Let’s consider an investor who just made ₹ 50 lacs in a real estate transaction. He is looking for a safe avenue to invest, before he takes a final decision on what to do with that money. An ideal scheme in this case would be a Liquid Fund, which is designed to provide liquidity with generally a high probability for capital protection. He can redeem whenever he has made up his mind.

Therefore, the decision on how long one needs to stay invested, depends on **investment** **objective**. Investors need to periodically review investment status and progress, with their advisors. During such reviews, decisions to redeem, switch, invest or leave alone are usually made.

# SIP or Lump Sum: How Should You Invest in Mutual Funds?

## ****1. Introduction****

There are two primary ways of [investing in a mutual fund](http://cleartax.in/save?ref=save-content-pages) — lump sum and SIP. A lump sum investment is a one-time investment while a SIP ([systematic investment plan](https://cleartax.in/s/sip)) is a recurring investment.

A lump sum investment is generally considered when the investor has a big corpus to invest. This could be money received after retirement or from the sale of a house or from an inheritance or it might just be the case that you have accumulated money in your bank account and wish to invest it now. There can be many reasons to consider a lump sum investment, but a SIP is generally recommended. This is more so in the case of investments in an [equity mutual fund](https://cleartax.in/s/equity-funds/).

## ****2. Benefits of SIP over Lumpsum Investments****

A SIP has the following benefits over a lump sum investment:

### No worry of timing the market:

The markets have always been volatile. Investors often face confusion regarding the best time to enter the market. If you invest a big amount in a market high and the markets crash after you have invested, you will lose out on a major portion of your investment.   
  
With a SIP, your money is spread over time and only some parts of your entire investment will be at a peak, which will allow you not only limit losses but also invest at a low with the next SIP installments

### Rupee cost averaging:

A SIP allows you to invest at different levels of the market. When the market is low, the fund manager will be able to buy more units as compared to when the market is at its peak. It will help to reduce the per-unit cost of buying the units. This phenomenon is known as [rupee cost averaging](https://cleartax.in/s/rupee-cost-averaging-works/). Ultimately, you will end up with higher gains.

### Build the habit of investing:

When you initiate a SIP, a fixed sum is transferred from your bank account to the mutual fund scheme. It is a disciplined way of investing and inculcates the habit of saving.  
  
The earlier you start, the larger the corpus that you may accumulate.

### Ideal for budding investors:

If you are someone who has just started a career, then SIP is your thing. You can begin investing and get exposure to equities even with a nominal amount. As your income increases in future, you may step-up your investments.

SIP investments can also earn higher long-term returns as compared to lump sum investments. You can still invest a lump sum amount in a debt fund, but SIPs are the way to go when it comes to investing in equity funds.

## ****3. How should you invest in mutual funds if you have a big corpus in hand?****

Let’s suppose you have ₹10 lakh in your bank account that you wish to invest in mutual funds for the long-term. You should surely not put the entire amount in equity funds in one go.

There are two approaches that you can take to invest this amount:

* Start a monthly SIP of an amount that you are comfortable with. This could be ₹10,000, ₹20,000 or ₹50,000. Let the money stay in your bank account till all of it gets invested systematically in the equity mutual funds you have chosen
* Invest the lump sum in a liquid fund. Then start a Systematic Transfer Plan (STP) from the debt fund to an equity fund. Your corpus will not only earn higher returns than a savings bank account but also allow for systematic investment.

If you want to go for an STP, then be aware of the tax implications.

## ****4. What are the rules of taxation on the gains made from such investments?****

Gains made from debt fund are subject to [capital gains tax](https://cleartax.in/s/different-mutual-funds-taxed/). Short-term gains are added to your taxable income while long-term gains are taxed at 20% after indexation. Every STP installment will be considered as a redemption from the debt fund and taxed accordingly. But despite the tax, the debt fund investments will generate higher returns than a bank account, especially if the STP to an equity fund runs for a long period of time. Investors who don’t want to complicate things can opt for the first option. But either way, a lump sum in an equity fund should be avoided.