Focus on a scheme's risks, too, not just its returns

Enquire how the high returns being promised will be generated, and whether you are comfortable taking the accompanying risk

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Two cases are currently in the news in which a large number of investors may lose their hard-earned money. One is that of a Mumbai-based stockbroker called Anugrah Stock & Broker, which allegedly promised its clients an assured monthly return by trading in futures and options (F&O), but was unable to do so as it suffered losses in the market. The second case is that of a Kerala-based entity that collected money from depositors, again by promising a high return of 18 per cent. With a large number of customers demanding their money back during the Covid crisis, the scheme collapsed. Both these cases are currently under investigation.

Norms for brokers tightened

The Securities and Exchange Board of India (Sebi) has taken many steps over the past year that will make it harder for brokers to cheat customers. The new norms on margin pledging, for instance, are expected to reduce misuse of clients' shares lying in demat accounts. "Earlier, the broker could transfer those shares to his own demat account for margin funding and possibly misuse them. Now the shares will remain in the client's account and a lien will be marked on them there itself," says Shrey Jain, founder, SAS Online, a Delhi-based discount broking firm. Auditing of brokers has nowadays become entirely focused on possible misuse of clients' shares and money.

Don't lower your guard: Despite tighter regulations, investors need to be on guard. "Check the monthly statement that comes from your depository. Also, keep your mobile number and email ID updated with the broker. If an unauthorised transaction happens, you will get an alert," says Jain.

If you are not trading, then don't leave excess money with the broker. Treat any delays in pay-outs as an early sign that the broker may be in financial trouble. Stick to brokers who just offer broking services and do not engage in proprietary trading. It is when brokers lose money in proprietary trading that they resort to misuse of clients' shares and cash.

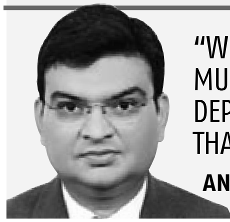
YOUR READY-TO-DEPLOY ANTI-FRAUD ARSENAL

Against broker shenanigans

- Stick to brokers who only offer broking service and don't engage in proprietary trading
- Don't fall for the promise of a fixed monthly return
- Use eDIS mechanism and avoid giving PoA to your broker. If you give PoA, it should be for pay-ins only, not for trading

Against Ponzi schemes

- Read the product document to understand how the returns will be generated. If the scheme seems improbable, stay away
- Don't invest based on recommendations of friends and relatives; do your own due diligence
- If you can't, pay a fee to a professional to do so on your behalf



"WHENEVER THE RATE OF RETURN BEING PROMISED IS MUCH HIGHER THAN WHAT BANK OR CORPORATE FIXED DEPOSITS AND DEBT MUTUAL FUNDS ARE OFFERING, THAT SHOULD ACT AS A RED FLAG"

ANKUR MAHESHWARI, CEO, Equirus Wealth Management

Avoid handing over trading rights: Under no circumstance should you give your broker the right to trade on your behalf. "Do not give the broker power of attorney (PoA) to trade. Even if you give PoA, it should be a limited-purpose PoA, which he may use to make pay-in (to transfer shares from your demat account to the exchange when you sell shares)," says Jain. It's best to use the electronic delivery instruction slip (e-DIS) facility.

F&O trading can't yield assured return: Do not fall for your broker's promise of a regular monthly return. "Futures and options are complex instruments that most retail investors should avoid. And equity as an asset class is not geared to deliver regular income. So, any promise of regular return where the underlying asset is equity is bound to fail," says Vishal Dhawan, chief financial planner, Plan Ahead Wealth Advisors.

Steer clear of Ponzi schemes

Kerala-based non-banking financial company Popular Finance was collecting deposits promising a high rate of return. "Whenever the rate of return being promised is much higher than what bank or corporate fixed deposits and debt mutual funds are offering, be warned," says Ankur Maheshwari, chief executive officer, Equirus Wealth Management. Investors need to understand that high returns are always accompanied by high risk. "Check where the risk lies and whether you are comfortable taking it. Investigate how the returns will be generated," says Dhawan.

Avoid following the herd: Do not buy financial products based on the recommendations of friends and relatives. A Ponzi scheme feeds on this very concept: Everyone entering the scheme assumes the person preceding him has done the due diligence. In the process, no do due diligence gets done.

Read investment documents before signing on the dotted line. If you do so, you may sometimes be able to spot the divergence between what you have been told (regarding how the returns will be generated) and what may actually be done with your money.

Beware of credit risk: At a time when many entities are under severe revenue pressure, be extremely conservative about where you invest. "Only deposit your money with the most blue-chip of public- and private-sector banks," says Avinash Luthria, a Sebi-registered investment advisor and founder, Fiduciaries. With returns on fixed-income investments falling (especially post-tax and post-inflation), investors are constantly looking out for avenues that will give them slightly higher returns. But in this quest, do not get tempted into investing into fraudulent or high-risk products. "Stay away from all grey areas. Once you venture into them, you will have to wrestle with the question of what is riskier and what is less so. In today's world, even financial professionals struggle to answer that question," says Luthria. He cites the example of Yes Bank's AT-1 bonds. Many knowledgeable people invested in them thinking the risks were manageable but ended up losing their principal. Luthria's advice for people falling short of their investment goals: Instead of trying to earn a higher return by investing in riskier products, raise your savings rate .

Finally, do the due diligence before entering any product. Even a basic Google search about Popular Finance would have revealed that the Reserve Bank of India had issued a warning about its activities. If you can't do the due diligence, pay a fee to a financial professional to vet the product on your behalf.